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SUBJECT: TELEKOM SERBIA SCANDAL GROWS, IMPLICATING EU COMMISSION PRESIDENT PRODI AND ITALIAN DIPLOMATS

1. Summary: Over the past several weeks, pro-Government daily "Il Giornale" published numerous articles on the 1997 sale by Telekom Serbia of a stake to Telecom Italy -- a ruinous financial speculation that helped keep Milosevic in power and allegedly involved kickbacks to several members of Italy's then-governing center-left majority, including current EU Commission President Prodi. Although Prodi and the others rejected the allegations as rightist propaganda, the rest of the press has recently picked up the story and calls for clarification are rising from Prodi's own political allies. Prodi and others have confirmed their willingness to testify before a parliamentary commission -- and maybe even judicial authorities -- investigating the scandal. End summary.

Igor Marini is arrested and talks

2. The "Il Giornale" stories stem from the arrest in Switzerland in May on charges of illegal financial dealings of an ex-financier, Igor Marini, who -- by his own account -- was materially involved in money laundering activities and the consignment of bribes in connection with the Telekom Serbia affair. Prior to his arrest, he was called to testify before the Italian parliamentary commission investigating the deal and the arrest occurred when Marini and four commission members traveled to Lugano to pick up some documents that he claimed would back his statements.

3. Marini has since been transferred to a Turin jail and is now also being questioned by Turin judicial authorities. According to "Il Giornale," and recently to the rest of the press, he is revealing an enormous amount of facts regarding alleged underhand dealings in connection with what was a secret agreement signed in June 1997 between Italy's then-public telecommunications company, Telecom Italy, and Telekom Serbia. Under that agreement, Telecom Italy bought 29 percent of the Telekom Serbia shares for 900 billion lire (roughly 450 million dollars). It then reportedly sold them back in February 2003 for less than half their original cost. Calculating an annual interest rate of 12 percent on the total sum, the parliamentary commission gauged a net loss for Telecom Italy of exactly 900 billion lire -- equal to the total cost of the original deal.

Igor says the left got kickbacks

4. According to "Il Giornale," the agreement with Telekom Serbia served to supply Milosevic's regime with direly needed fresh cash, at a moment when Italy's international allies were preparing to clamp down on Milosevic because of Kosovo. Reportedly, Marini told the judicial authorities and the parliamentary commission that bribes were paid in connection with the deal to, among others, then-PM Romano Prodi (an expected challenger to PM Silvio Berlusconi in the next national elections), then-FM (and current Senate Vice President) Lamberto Dini, and then-MFA Under Secretary for the Balkans (now head of the largest center-left opposition party, Democrats of the Left, DS) Piero Fassino.

Bascone said "watch out"

5. "Il Giornale" cited one of fourteen letters and cables by the then-Italian Ambassador to Belgrade and current Deputy Director of the MFA Europe Bureau Francesco Bascone to then-MFA U/S Fassino, in which Bascone underscored his strong concerns over the deal. Bascone reportedly cautioned against possibly getting involved in money laundering activities, highlighted the "illegitimacy of the acquisition," and warned against "scandals on the improper use of fresh moneys from Italy." He also noted that the funds "would be at the direct disposal of Milosevic and of his power group" and "the danger cannot be ignored." He said, "the government must assess if the economic and political benefits are greater than the dangers." Bascone repeated much the same statements when he was heard by a parliamentary

commission several months ago.

Sannino said Bascone said

16. In addition, "Il Giornale" reported the involvement of another Italian diplomat, Counselor Stefano Sannino. Prior to the events, Sannino was First Secretary in Belgrade, and during them he was Chief of Secretariat to then U/S Fassino. Sannino is at present EU Commission President Prodi's Personal Representative to the G8 and his cabinet adviser on external relations, foreign trade, and security and defense. Sannino reportedly stated before the parliamentary commission that Bascone had fully informed Fassino of the deal before the contract was signed and that Fassino had fully briefed then-FM Dini. Sannino specifically said he was not aware of Prodi's ever having been informed.

Vattani did not know?

17. The press did not dwell on a third diplomat who was also questioned by the commission some months ago, Umberto Vattani, then Dini's Chief of Cabinet, later MFA Secretary General, and currently Italy's Ambassador to

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the EU. However, Vattani was cited in the Italian news agency ANSA as denying ever having been informed of the affair, saying he had learned about it later in the press, and claiming that Bascone's statements were "totally false."

The story is old

18. The Italian public first became aware of the deal in February 2001, when center-left, independent daily "La Repubblica" disclosed the story. Then-FM Dini told Parliament at that time that neither the MFA nor the Treasury Ministry -- Telecom Italy's controller -- had been informed in advance that Telecom Italy was concluding the deal, nor were they provided information afterward. According to Dini, there was no technical reason for Telecom Italy to inform the government, because Telecom Italy was buying minority shares and would have no control over the decisions of Telekom Serbia. Telecom Italy could legally make its own decisions, in particular because it was not violating any sanctions, he said. He said that, when the deal was signed, EU, U.S., and UN sanctions against Serbia had already been lifted and the general feeling following the November 1995 Dayton Agreements was that the international community had to prepare the groundwork for a normalization of relations with Serbia. Milosevic had started a privatization plan and many foreign companies, including U.S. companies, had begun negotiating with Belgrade. Dini remarked that the "Repubblica" allegations seemed to be the work of "CIA blue collar workers." The story died there until the "Il Giornale" articles this summer, where Dini's reference to the CIA was put into context: he thought the previous U.S. Administration had passed the story to the press to get back at him for allegedly being pro-Serbian. (Note: Some papers have reported that Dini's wife, an independent businesswoman, was a beneficiary of the kickbacks.) Former U/S Fassino now reportedly claims that the U.S. in 1996-1997 was encouraging other nations to invest in Serbia.

Bob Gelbard has something to say

19. Robert Gelbard, the Clinton Administration's Special Envoy for the Balkans, refuted Fassino's claim as "ridiculous" and "totally false," in an interview in the wide-circulation, centrist news weekly "Panorama." He remarked, "Washington had no reason in the world to encourage companies to give money to Milosevic: we wanted investments in Bosnia, certainly not in Serbia." According to Gelbard, the deal between Telecom Italy and Telekom Serbia negatively affected U.S.-Italy relations for a while, even though it did not dent their soundness. "That mountain of Italian money gave Milosevic a breath of air and allowed him to buy new loyalties and continue to pay the military's wages," he said. He added, "The news of the Italian investment, in fact, was received with serious concern by the U.S. government. We had reasons to believe that the agreement contained some illegal elements."

Prodi and the others want to testify

¶10. Prodi, Fassino, and the other individuals involved initially reacted with heated indignation, characterizing financier Igor Marini as a "lying imbecile" and a "braggart." But the scandal is not going away this time and denying involvement seems not to have helped those fingered. Some of the leftist press and even some leftist politicians are beginning to doubt the innocence of those allegedly involved and are beginning to demand public explanations. In an open letter to the press August 27, Prodi said he wants to be heard by the commission as soon as possible and will tell the commission he had never been -- as there was no reason he should have been -- informed of the deal until after it happened. In press statements the same day, all the others named in the press stated their intention to testify before the commission. Some have even indicated their availability to be heard by the Turin magistrates.

European Parliament also interested in Prodi's activities

¶11. In addition, "Il Giornale" reported that Prodi is coming under fire at the European Parliament, where he has been asked to answer formal queries about his involvement in the Telekom Serbia affair, as well as in the EUROSTAT scandal, in which two high-level EUROSTAT officials are under judicial investigation in a French court on charges of having taken approximately 900 million euros from EUROSTAT funds. (Note: EUROSTAT is the EU Commission's statistics agency. End note.) Instead of firing the officials, Prodi has reportedly reassigned them to other positions within the Commission.

¶12. Comment: Accusations and denials of wrong-doing by politicians played out in the Italian press are everyday occurrences in Italy, and it is unlikely that the current resurgence of interest in the Telekom Serbia deal will keep Prodi from completing his mandate and term as EU Commission President. He has promised to return to Rome when his current tenure is finished, in November 2004, and is considered a virtual shoe-in as the center-left's candidate to run against Berlusconi as Prime Minister in the next national elections. It is at that time that these most recent allegations may return to haunt him.

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